BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 96-168-W/S - ORDER NO. 2000-713

SEPTEMBER 1, 2000

IN RE:	Application of Kiawah Island Utility, Inc. for Approval of an Increase in its Rates and Charges for Water and Sewer Services.	)))	ORDER ON REMAND APPROVING 1996 RATES AND CHARGES

This matter comes before the Public Service Commission of South Carolina (the Commission) on remand from the South Carolina Supreme Court, and by way of an Application filed on behalf of Kiawah Island Utility, Inc. (the Company or Kiawah) for approval of a new schedule of rates and charges for its water and sewer customers on Kiawah Island in Charleston County, South Carolina. The Company's July 9, 1996 Application was filed pursuant to S.C. Code Ann. Section 58-5-240 (Supp. 1995), as amended, and R.103-821 of the Commission's Rules of Practice and Procedure. We subsequently issued Order Nos. 97-4 and 97-151 in this Docket. The South Carolina Supreme Court ultimately reversed the March 10, 1998 Order of the Honorable J. Derham Cole, Circuit Court Judge, which had affirmed our Orders, and remanded the entire case back to this Commission to more fully explicate our findings. Accordingly, we issue the present Order in place of Order No. 97-4 and 97-151.

By letter, the Commission's Executive Director instructed the Company to publish a prepared Notice of Filing, one time, in a newspaper of general circulation in the area affected by the Company's Application. The Notice of Filing indicated the nature of the

Company's Application and advised all interested parties desiring participation in the scheduled proceeding of the manner and time in which to file the appropriate pleadings. The Company was likewise required to notify directly all customers affected by the proposed rates and charges.

Petitions to Intervene were filed by the Kiawah Property Owners Group, Inc. (KPOG), the Consumer Advocate for the State of South Carolina (the Consumer Advocate), and the Town of Kiawah Island (the Town).

The Commission Staff (the Staff) made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the Company's operations. The other parties likewise conducted their discovery in the rate filing of Kiawah.

A public hearing relative to the matters asserted in the Company's Application was held on December 2, 1996 in the Hearing Room of the Commission at 111 Doctors Circle, Columbia, South Carolina. Pursuant to S.C. Code Ann. Section 58-3-95 (Supp. 1995), a panel of three Commissioners composed of Commissioners Saunders, Scott, and Bradley was designated to hear and rule on this matter. Lucas C. Padgett, Jr., Esquire, represented the Company; Michael A. Molony, Esquire, represented KPOG; Elliott F. Elam, Jr., Esquire, represented the Consumer Advocate, and John M.S. Hoefer, Esquire, represented the Town. The Staff was represented by F. David Butler, General Counsel.

The Company presented the direct and rebuttal testimony of Townsend P. Clarkson, and the direct and rebuttal testimony of James Mitchell Bohannon, III. KPOG presented the testimony of Wendy K. Kulick, J. Richard Sayers, and Wallace R. DuBois.

The Consumer Advocate presented the testimony of Philip E. Miller. The Staff offered the testimony of D. Joe Maready and Robert W. Burgess.

FINDINGS OF FACT

1. The Company is a water and sewer utility operating in the State of South Carolina and is subject to the jurisdiction of the Commission pursuant to S.C. Code Ann. Section 58-5-10 (1976) et. seq. Kiawah Island Utility, Inc. is owned by Kiawah Resort Associates, L.P. (KRA).

2. The Company (as of the hearing date) provided water service to 2,696 residential and commercial customers and sewer service to 2,386 residential and commercial customers on Kiawah Island, Charleston County, South Carolina.

3. The Company purchases its water from St. Johns Water Company, Inc. The Company (as of the hearing date) had three ground level storage tanks with a capacity of 4.5 million gallons, along with support equipment for the pumping and metering of the water supply and distribution system. The Company's sewer system (as of the hearing date) was comprised of gravity collection mains, force mains, and treated effluent transfer mains, aggregating approximately 58 miles, 37 sewage pumping stations, and a wastewater treatment facility.

4. The Company's prior rates and charges were approved by Order No. 92-1030, dated December 15, 1992, in Docket No. 92-192-W/S.

5. As of the hearing date, the Company had six rate schedules relating to its water and sewer charges and conditions and other miscellaneous service charges. The Company's residential water service charge was $18.00 per month for a minimum bill of

0 to 3,000 gallons. All water consumed over 3,000 gallons per month was billed at a rate of $1.80 per 1,000 gallons. The Company charged a flat rate for residential sewer of $22.00 per month. The Company's tap fees were $500 for both water and sewer for residential customers. Tap fees and Basic Facility charges were based on meter size for the other classes of customers. These were rates adopted in 1992.

The Company's 1992 rates and proposed 1996 rates are depicted in Hearing Exhibit No. 8, Exhibit A of the Water and Wastewater Department's exhibits in the Commission Staff Report. In lieu of discussing all of the 1996 proposed changes in the Company's six rate schedules, the Commission will highlight the changes requested to the Company's residential service rates and terms of service. The Company proposed for 1996 to increase the residential water service charge to $21.00 per month for a minimum bill of 0 to 2,000 gallons. All water consumed over 2,000 gallons per month would be billed at a rate of $2.10 per 1,000 gallons. The Company proposed to increase its sewer service charge to a flat rate of $26.00 per month. In addition, the Company proposed to raise its tap fees for both water and sewer to $600 for residential customers. The Company also proposed various changes in its other schedules.

6. The Company asserts that the 1996 requested rate increase was required because of several reasons. First, according to Company witness Clarkson, Kiawah has incurred increased costs associated with purchased water from St. John's Water Company. The cost of water purchased from St. John's Water Company increased from $1.34/thousand gallons to the current rate of $1.46/thousand gallons, an increase of 9%, according to the Company. The total cost of water, inclusive of Operation and

Maintenance and leakage, rose from $1.37/thousand gallons to $1.63/thousand gallons, which represents a 19% increase. Tr., Vol. 1, Clarkson at 25. Further, according to Clarkson, the Company undertook several significant capital improvement projects to enhance the water and wastewater systems, such as telemetry of major irrigation systems, improvements to the water pumping/storage and wastewater treatment/storage facility, improvements to the St. Johns transmission system and storage facility, cost associated with installing sewer on Eugenia Avenue, plus the purchase of transmission lines from KRA. Further, the Company increased its commitment from NationsBank. The increases in plant and equipment, according to Clarkson, significantly altered the Company's financial position. Tr., Vol. 1, Clarkson at 24.

7. The Company proposed that the appropriate test period to consider its requested increase was the twelve-month period ending December 31, 1995. The Staff concurred in using the same test year for its accounting and pro forma adjustments. The Intervenors did not contest the test year.

8. The Company sought an increase in its rates and charges for water and sewer service which would result in an operating margin of 5.43%. Tr., Vol. 1, Clarkson at 25.

9. Under the Company's 1992 approved rates, the Company stated that its operating revenues for the test year, after accounting and pro forma adjustments, were $2,650,861, a figure supported by the Consumer Advocate. We adopt this amount as an appropriate statement of operating revenues, prior to any proposed increase. The

Company sought an increase in its rate and charges for water and sewer service in a manner which would increase is operating revenues by $484,369.

10. The Company asserts that under its 1992 approved rates, its total operating expenses for the test year, after accounting and pro forma adjustments, were $2,920,816. Tr., Vol. 1, Clarkson at 33. Staff concluded that the Company's operating expenses for the test year, after accounting and pro forma adjustments, were $2,243,049. See Hearing Exhibit 7. However, for the reasons explained below, we hold that the total expenses, as explained below, were $2,248,827. The Company, the Staff, the Consumer Advocate, KPOG, and the Town of Kiawah all proposed certain adjustments to the Company's books and records, which are explained in some detail below.

11. Under the 1992 rates, the Company's net operating income was $402,034. Applying customer growth of $7,076 and interest of ($487,809), the Company's Total Operating Income is ($78,699), yielding a (2.97%) operating margin. See Hearing Exhibit 7.

12. The Commission has determined that the appropriate Total Operating Income for the computation of the operating margin is $102,360. See Hearing Exhibit 7.

13. The Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and the fixing of just and reasonable rates.

14. A fair operating margin that the Company should have the opportunity to earn in this case is 3.55%, which is produced by the appropriate level of revenues and expenses found reasonable and approved herein.

15. This operating margin is produced through additional revenues of $235,338, for a total revenue under the 1996 rates of $2,886,199. The Commission approves $57,410 in additional expenses for total expenses of $2,306,237. Net Operating Income of $579,962 is then produced. Applying customer growth of $10,207 and an interest adjustment of ($487,809), Total Operating Income is $102,360.

16. The rate designs and rate schedules approved by the Commission as described herein are appropriate and should be adopted for the 1996 rates.

17. The rates and charges depicted in Appendix A, attached hereto and incorporated by reference, are approved for the 1996 rates.

EVIDENCE AND CONCLUSIONS

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2, 3, AND 4.

The evidence supporting these findings concerning the Company's business and legal status, number of customers, water purchasing practices, and the Company's last rate increase are contained in the Company's Application and in prior Commission Orders in the docket files of which the Commission takes judicial notice. The Company is a water and sewer utility under S.C. Code Ann. Section 58-5-10 and is providing water and sewer service in its approved service area in Charleston County, South Carolina. The Company's operations and subject to the jurisdiction of this Commission. These findings of fact are essentially informational, procedural, and jurisdictional in nature, and the matters that they involve are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 5 AND 6.

The evidence supporting these findings of fact are included in the Company's Application and Company testimony presented at the hearing. Many of the matters contained therein were hotly contested by the parties, and more discussion will appear infra thereon.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NO. 7.

The evidence for this finding concerning the appropriate test period is contained in the Company's Application and in the testimony and exhibits of the Company witnesses, the witnesses for the intervenors, and the Staff's witnesses. The Company proposed in its Application that the appropriate test year by which to consider the requested rate increase was the twelve month period ending December 31, 1995, and based the filing on that time period. Relying on the Company's proposed test year, the Staff and the witness for the Consumer Advocate utilized the same test period for their accounting and pro forma adjustments.

A fundamental principle of the ratemaking process is the establishment of a historical test year period. While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year changes in expenses, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. See Parker v. South Carolina Public Service Commission, 280 S.C. 310, 313 S.E. 2d 920 (1984), citing City of Pittsburgh v. Pennsylvania Public Utility Commission, 187 P.A. Super. 341, 144 A.2d 648 (1958);

Southern Bell v. The Public Service Commission, 270 S.C. 590, 244 S.E.2d 278 (1878). Based on the record, the Commission finds the twelve month period ending December 31, 1995, to be the reasonable and appropriate period for which to make its ratemaking determinations herein.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NO. 8.

The evidence supporting these findings of fact are included in the Company's Application and Company testimony presented at the hearing, more of which will be discussed below.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 9 THROUGH 12.

The Commission believes that the Company should receive an additional $235,338 in revenue in this case.

With regard to adjustments to operating revenue and expenses, the Commission would discuss the following:

(A) Management Fees

In its testimony, the Company proposes the inclusion of approximately $100,000 in management fees as direct labor cost and overhead, which would recognize a contract for management fees between the utility and KRA. There is no dispute that this amount was paid, however, there is a significant dispute regarding whether or not the fee is reasonable for ratemaking purposes. The Consumer Advocate opposes inclusion of the management fees as being unreasonable for ratemaking purposes. The Staff and KPOG have taken the position that an adjustment of ($64,000) is appropriate, even though KPOG also takes an alternate position that the entire amount should be excluded.

In Kiawah's prior rate case, Docket No. 92-192-W/S, in Order No. 92-1030, dated December 15, 1992, a similar Company proposed management fee was discussed, and it was noted that the information and proposed adjustment was not supported by time sheets. The Commission held in that Order, that "in the future, if the Company wishes to present similar information concerning the allocation of such costs to the utility company, time sheets and appropriate records should be maintained and available for inspection." We note that in the present situation, the Company provided Staff with time sheets of the employees of the parent company, but did not include time sheets for the partners or the Board of Directors. Therefore, we hold that the Company has not proven the reasonableness of its entire proposed management fee of $100,000, since it has furnished only incomplete information, even though it did attempt to further support its claim through the answering of Consumer Advocate Interrogatory No. 2-16 near the hearing date.

Beyond this, there seems to be considerable duplication between the services which are supposedly provided by the parent company and the direct cost incurred by the Company. Consumer Advocate witness Miller noted that the Company has a manager, an assistant manager, and a controller on its payroll. During the test year, these three employees received salaries of $111,124. The Company also incurred audit and tax fees of $23,749. Yet a review of the services provided by the parent company seem similar in nature to those which should be handled by the Company's in-house employees or by services provided by other outside professionals. See Tr., Vol. 2, Miller at 155 - 156 and Hearing Exhibit 6, Attachment 2.

In any event, as noted by the Supreme Court in Hilton Head Plantation Utilities, Inc. v. The Public Service Commission of South Carolina, 312 S.C. 448, 441 S.E. 2d 32 (1994), an allowance of charges arising out of intracompany relationships may be properly refused when there is an absence of data and information which would allow the Commission to ascertain the reasonableness of the cost incurred. We hold in this case that, indeed, the Company has not furnished sufficient data to ascertain the reasonableness of the entire management fee amount. Since some data was provided, we do hold that the Company has justified $36,000 of the fees by its submissions of proof. Therefore, we adopt Staff's and KPOG's adjustment of ($64,000). See Tr., Vol. 2, Maready at 197.

It should be noted that we had no sufficient way of gauging participation by the partners and/or directors of the parent corporation in this case. We do not believe that the methodology employed by the Company in the answer to the Consumer Advocate interrogatory was acceptable. After some consideration, we do hold, however, that time sheets will not be required in future cases to show hours spent on utility business by upper management of the parent corporation, but that some other method be employed for gauging these hours, should the Company ask for a similar level of management fee, based partially on hours spent on utility work by upper management.

(B) Salaries and Benefits

We note that Staff has proposed to annualize salaries at October 16, 1966, and, accordingly, proposed an adjustment of $47,736. No other party proposes such an adjustment. We must deny the proposal, since it is too for outside the test year to be a

reasonable post-test year adjustment. We adopt the Consumer Advocate's amount of $367,301 as being the appropriate amount for salaries and benefits.

(C) Repairs and Maintenance

With regard to tank painting, we note that, during the test year, the Company paid for its share of painting the water tank on Johns Island in the amount of $43,014. Various parties took into consideration the number of tanks necessary for rendering service, and developed proposals for various amortization periods. Staff proposed a 3 year amortization, and, accordingly, an adjustment of ($28,676). The Consumer Advocate proposed a 5 year averaging of the repairs and maintenance expense account, and therefore, a ($32,111) adjustment. KPOG proposed to amortize the painting over 6 years, with an adjustment of ($35,846). We have examined these proposals and believe that all have merit. However, we hold that the Consumer Advocate's proposal is a good balance of the interests of the ratepayers and the Company. We therefore adopt a 5 year average expense period with a ($32,111) adjustment to repair and maintenance expense.

(D) Rate Case Expense

The Company proposes to increase is professional fees by $10,826 in order to reflect the amortized amount of rate case expense that the Commission allowed in its previous case. The Staff proposes a 3 year amortization of actual expenses incurred through October 4, 1996, and therefore, an adjustment of $4,224. The Consumer Advocate opposes these adjustments and recommends that the Commission reject them. The Consumer Advocate asserts that although the Commission allows for the recovery of rate case expense incurred when seeking an increase in rates, the recovery should be

based upon the actual costs associated with this proceeding, and not the previous one. Tr., Vol. 2, Miller at 158 and Vol. 2, Maready at 198. Witness Miller also testified that in order to determine a normal level of rate case expenses, it would be appropriate to determine the rate case costs which have been incurred subsequent to the last rate case, including the costs associated with this proceeding, and to normalize those costs. However, the Consumer Advocate noted that since the Company had not provided the Commission with this data, it was not possible to quantify a reasonable adjustment. Tr., Vol. 2, Miller at 158. Although the Company did provide the requested data the day of the hearing, this data had not been reviewed by the Staff. Further, the Company failed to bring its actual expenses up to date as suggested by the Staff in its testimony. Tr., Vol. 2, Maready at 198. Because of all these reasons, the Commission adopts the Consumer Advocate's recommendation and rejects the Company's rate case expense adjustment, as well as the Staff's.

(E) Telemetering and Eugenia Avenue

Consulting and Legal Fees

Staff proposed to amortize telemetry and Eugenia Avenue consulting and legal fees over three years, and telemetering legal expenses over three years as well. The proposed adjustments were in the amounts of ($13,579) and ($4,365) respectively. We hereby reject these adjustments as not being appropriate or necessary for such small amounts as are seen here.

(F) Engineering Consulting Fees

Various parties had different proposals with regard to Engineering Consulting Fees in order to capitalize said fee. The Company proposed a 3 year average and an adjustment to Operation and Maintenance (O & M) Expense of ($46,790). The Staff proposed an adjustment to Depreciation Expense of $1,935 and an adjustment to O & M expense of ($82,335). The Consumer Advocate proposed a 5 year average, and therefore, an adjustment to O & M expense of ($72,131). We adopt the Consumer Advocate's adjustment. This approach gives the maximum ratepayer benefit of all of the proposed approaches, and, on balance, is the best approach.

(G) Lawsuit Expenses for Fire Losses

Both the Staff and the Consumer Advocate propose to defer lawsuit expenses for fire losses, and, therefore, propose an adjustment of ($26,265). As shown in testimony, the lawsuit is continuing and these expenses are not really known and measurable at the time of this case as to what the final amount will be. Therefore, we believe that deferral is appropriate and adopt this adjustment.

(H) Sludge Removal

In its Application, the Company increased other operating expenses by $50,000. According to the Company, this amount approximates a three year average cost to remove sludge from holding cell #3. However, based upon bids received subsequent to the filing of the application, the estimate has been revised to $97,612. See Tr., Vol. 2, Maready at 220-221. KPOG recommends a 10-year amortization of updated estimated

expenses and therefore an adjustment of $9,761. Both the Consumer Advocate and the Staff recommend rejection of both proposals. It is clear from the Company's testimony that the amounts given are far from the final amount of the contract. Second, the sludge contained within the cell is an accumulation over many years and it would be unfair to ratepayers to include the total amount in one lump sum. Based on this information, we adopt the position of the Consumer Advocate and the Staff, and reject the Company's and KPOG's proposals.

(I) Rental Expense

Both the Staff and KPOG recommend a ($33,000) adjustment to remove from allowable expenses rental expense on a lease agreement not approved by the Commission. In addition, KPOG proposes that the Commission rescind the Lease agreement, plus an additional lease agreement for the Down Island Storage facility. We decline to order rescission of the two leases, and we reject the proposed adjustment. We agree that the better practice for the Company in this instance would have been to have this Commission approve any lease agreements, pursuant to our Regulations 103-541 and 103-743, however, the lease in question was for property that was certainly used and useful in the provision of service by the Company. We will therefore reject Staff and KPOG's adjustment. However, we caution the Company to seek pre-approval of such leases in the future, in compliance with the Regulations. Failure to do so in the future may cause a rejection by this Commission of expenses attributable to such leases.

In further support of our conclusion, we would point out that the testimony of Mr. Bohannon, the Utility's engineer, was that his firm, Thomas & Hutton, had studied

several alternatives on how to increase additional storage capacity, which was needed to hold treated effluent from the wastewater treatment. DHEC requires the treated wastewater to be disposed of by spraying on the golf courses at the rates approved by the Commission. Tr., Vol. 2, Bohannon at 10, 17 - 19.

Mr. Clarkson testified that the Utility had to have additional storage for the treated effluent. Thus, Thomas & Hutton prepared an analysis of the alternatives for increasing the storage capacity. These alternatives were much more expensive than the construction of an additional storage lagoon, so KRA offered to lease its adjoining property for expansion of the storage facility. Tr., Vol. 1, Clarkson at 93-96.

The adjoining property was appraised by the independent appraisal firm of Attaway Thompson & Associates of Charleston. KPOG did not introduce any proof to contradict the real estate values set forth by Attaway Thompson & Associates. The only proof in the record is that the fee simple value of this property was determined to be $550,000. The testimony also established that it would have been difficult, if not impossible, for the Utility to borrow any additional money from the bank to purchase the property. Therefore, Attaway Thompson & Associates was requested by Mr. Clarkson to determine the fair market rental lease value for the property. Tr., Vol. 1, Clarkson at 103-104.

Once the lease value was determined by Attaway Thompson & Associates, the Utility Company entered into a five year lease with two options for a total fifteen (15) years. The base annual rental is $66,000 per year. The $33,000 approved by us as an expense in this case, was a half year's rental value.

KPOG does not challenge that an additional storage cell was necessary. Instead, Mr. Sayers expressed Petitioner's feeling that the holding cell property should have been donated to the Utility by KRA at no cost and that no rent should be allowed, regardless of the market value of these parcels. Tr. Vol. 2, Sayers at 52.

The issue here is one of fairness and reasonableness of the charges. The Utility's uncontradicted proof of the reasonableness and fairness of these rental expenses easily satisfied its burden of proving that the lease expense with its parent company is reasonable. See Hilton Head Plantation Utilities, Inc. v. The Public Service Commission of South Carolina, 312 S.C. 448, 441 S.E.2d 321 (1994).

(J) Depreciation Expense

The Company, the Consumer Advocate, and the Staff all propose various adjustments to depreciation expenses. The Company decreased the test year depreciation expense by $32,323. The Staff propose to annualize depreciation expense at December 31, 1995, whereas the Consumer Advocate suggests that depreciation be reduced for tap fees received for 1992 through 1995. The Company's amount reflects a reduction of $33,284 relating to contributions in aid-of-construction and an addition of $961 associated with the capitalization of meters, materials, and supplied related to the tap-in expenses which were capitalized for ratemaking purposes. According to the Consumer Advocate, the $33,284 reduction proposed by the Company is simply a carry forward of the adjustment that the Commission ordered in the last rate proceeding. The Consumer Advocate notes that in that proceeding, the rate base was determined as of December 31, 1991. The Consumer Advocate believes that subsequent to that time, the Company has

collected another $363,500 in tap-in revenues. The problem, as presented by Staff, is that it is concerned that not all of the capital costs associated with the tap-ins have been included on the Company's books, therefore, the Staff proposal to annualize depreciation expense at December 31, 1995 makes logical sense, and we adopt it. The adjustment would appear as a ($29,733) adjustment to accumulated depreciation and a $29,733 adjustment to depreciation expense.

With regard to the recognition of depreciation on completed 1996 addition, the Company recommends an adjustment of ($68,883) to accumulated depreciation. The Staff recommends an adjustment of ($61,700) to accumulated depreciation and $61,700 to depreciation expense. The Consumer Advocate does not believe that such depreciation should be recognized. We conclude that Staff's proposed adjustment most properly recognizes the depreciation at issue. We believe that recognizing such expense attributable to 1996 is consistent with our Court-mandated adjustments for post-test year occurrences that are known and measurable.

With regard to further depreciation expense, the Staff proposes an adjustment to exclude depreciation on a portion of Ocean Course to comply with our Order No. 92-1030. Using the methodology in that Order yields an adjustment of ($7,118). We adopt the Staff's adjustment, based on the Staff's following our mandate given in Order No. 92-1030.

(K) Capital Structure

The Company and Consumer Advocate propose that the Company's capital structure of December 31, 1995 be adopted. The Staff recommends the use of the

Company's capital structure at September 30, 1996. We have adopted, as a rule, the very latest capital structure available from a Company, because of the need for the most up-to-date and accurate figures. For this reason, we adopt the Staff's proposed capital structure as of September 30, 1996.

(L) Interest Expense

The parties have proposed a variety of interest adjustments based on multiple factors. The Company proposes an adjustment of $527,623, whereas the Staff proposes $487,809, and the Consumer Advocate $341,400. The interest expense is based on Staff's calculated rate base, and we will adopt Staff's number, since we have adopted Staff's rate base adjustments. See below.

(M) Customer Growth

The Commission has long recognized the need to adjust the test year amounts in order to account for customer growth. Consumer Advocate witness Miller testified that in order to produce an appropriate revenue requirement, the test year operating income must be measured against rate base which generated it. Miller concluded that rate base is determined as of December 31, 1995, but that the test year revenues are realized over the twelve month period ending the same date. Therefore, in Mr. Miller's opinion, a mismatch occurs. In order to eliminate this mismatch, the operating income, according to him, should be adjusted to incorporate revenues and expenses which would be realized on a basis of the actual investment at year end. According to Miller, a reasonable method of making this determination, and to eliminate the mismatch, is to annualize revenues and the associated expenses to reflect the growth in customers by comparing the year-end

customer levels with the average customer levels during the test year. Also, according to Miller, by using customer levels at year-end, the revenue requirement computation will consider the revenues associated with the customers at the year-end as well as the investment required to provide service to these customers.

The Company and Staff use a growth factor which is determined as a basis of the growth between average customers and year-end customers. The Consumer Advocate even states that if applied correctly, this formula might eliminate the mismatch of operating income with rate base. According to Miller, however, neither the Company, nor the Staff have applied the formula correctly, since they simply multiplied the formula against the operating income, thereby making the assumption that all Company expenses are going to increase proportionately to the increase in revenues.

We agree with the Consumer Advocate witness Miler when he states that the formula utilized by the Company and Staff assumes that all expenses are going to grow proportionately to the growth in revenues. We believe also that all expenses are going to grow proportionately to the growth in revenues. We do not believe that the Consumer Advocate's method is necessary or desirable in this case.

In the present case, the Commission would note that in Order No. 96-879, the Commission specifically stated that, for that proceeding, the Commission believed that the method proposed by the Consumer Advocate was a better one by which to calculate customer growth. The Commission recognized in that Order that the customer growth adjustment proposed by the Consumer Advocate was more "aggressive," and was appropriate, given the testimony in that case. In that case, there was testimony from the

Mayor of Tega Cay concerning the growth of Tega Cay, which the Commission believed justified the use of the Consumer Advocate's more "aggressive" customer growth adjustment.

In the present case, no such testimony was presented. Therefore, we clearly saw no reason to adopt the more "aggressive" method proposed by the Consumer Advocate, since no comparable testimony as was given in the Tega Cay case was presented here. Our decision is based on differing factors between the two cases. We therefore adopt the customer growth methodology used by the Company and Staff in this case. Staff's adjustment is $10,207, which we hereby adopt.

(N) Gross Receipts Taxes on Increase

The gross receipt taxes on the realized increase is simply calculated by multiplying 1.1% times the $235,338 granted in this case. This figure comes to $2,589.

(O) Remaining Legal Expenses

The Consumer Advocate proposes to adjust remaining legal expenses to a five (5) year average and proposes a ($10,073) adjustment. KPOG proposes to amortize total 1995 legal expenses over a three (3) period, and therefore proposes a ($25,918) adjustment. We have examined this matter, and believe that a five (5) year average most benefits the ratepayers of South Carolina, so we therefore adopt the Consumer Advocate's adjustment.

(P) Unidentified Assets

KPOG proposes to adjust Interest Expense and Long-Term Debt due to "unidentified assets" from the last rate case. The proposed adjustments are ($91,562) to

Interest Expense and ($1,251,550) to Long Term Debt. We have fully examined the KPOG testimony in the matter, but we are not persuaded that any change is in order. We accomplished what KPOG requests in Order No. 92-1030. We therefore reject KPOG's proposed adjustments in the present case.

First, KPOG's use of the term "unidentified assets" is a misnomer. In 1992, KRA, which is the sole shareholder of the Utility, sold lines, equipment, and other plant in service to the Utility. The Petitioner challenged expenses of the Utility related to this challenge in the 1992 rate case. It argued that all the assets which were sold to the Utility either had been previously given to the Utility by the parent company or should be donated by it without charge to the Utility. The Utility justified the payment by asserting that the assets conveyed were critical to its water and sewer system, in use, and had not been donated in the past at no charge.

In the 1992 case, this Commission recognized only that portion of the acquisition cost that could be linked to particular assets that had, without a doubt, never been transferred or donated to the Utility by the developer. For ratemaking purposes, this Commission denied this expense for any of the assets where there was the least uncertainty about whether they possibly could have been donated in the past. Contrary to what KPOG intimates in this case, all of these assets that were acquired from the parent company were identified by engineer and other witnesses as actually existing and being in service. What was "unidentified" was the paperwork disproving a contribution of a portion of these assets by the parent corporation to its subsidiary. No expense was allowed for these assets.

KPOG urged this Commission to adjust Interest Expense (by $91,562) and Long Term Debt (by $1,251,550) due to the "unidentified assets" from the 1992 rate case. In addition, KPOG also urges this Commission to go back, overturn our 1992 Order, and require the developer to pay $891,660 to the Utility that was excluded by the Commission from the rate case in the 1992 Order.

The applicable portion of Commission Order No. 92-1030 dated December 15, 1992, follows:

> (A) Asset Transfer - The Company and the Commission Staff agree that all of the assets evaluated by the Thomas & Hutton study should be transferred to the utility in the amount of $1,750,000.00. However, the KRG brought to the Commission's attention that a substantial portion of that amount could not be adequately identified. While the Commission does not agree with the KRG that these assets were 'phantom assets,' the Commission is of the opinion that for ratemaking purposes, these assets were not identifiable as to whether or not they had been previously donated to the utility company by the predecessor parent, or whether or not they still existed on the parent company's books. **It is uncontradicted in the record that the assets existed and were known from an engineering and accounting standpoint.** However, the Commission is of the opinion that the utility company's ratepayers should not be responsible for paying for assets that cannot be properly identified on either Company's books. Therefore, the amount of $891,660 which was identified by the Thomas & Hutton study as 'unidentifiable,' **will not be allowed in the Company's rate base for ratemaking purposes**. Therefore, only $858,340 will be placed into plant in service by the Company and $891,660 will be eliminated.
>
> Pages 24-25, PSC Order No. 92-1030, December 15, 1992 (emphasis added).

As is plainly apparent from this excerpt from the unappealed 1992 Order, this Commission did not impose on the ratepayers any financial expense whatsoever for paying any of the acquisition cost of $891,660. Instead, we excluded this expense of $891,660 from the rate base. There was no evidence in the record before the Commission in this case that this $891,660 was included in the rate base by the Utility. It was not.

No new evidence was presented on this issue in the current case. The same issue and argument were fully presented by KPOG to the Commission in the 1992 rate case. No appeal was taken from that decision. In this case, we reviewed the testimony presented and found no justification to modify our 1992 Order.

It should be noted that, if a company cannot recognize certain assets, it cannot keep them on the books [for ratemaking purposes]. Therefore, the Company deducted $445,000 from water assets, and $445,000 from sewer assets, and removed them from the books. This methodology was approved in Order No. 92-1030, and is likewise appropriate in the present case as well.

The Utility exactly followed the Commission's 1992 Order in removing the $891,660 in assets from its books for ratemaking purposes. This Commission in its 1992 Order, at page 25, also excluded all interest in connection with the unidentified assets. There is no evidence in this case that the Utility has included any of the $891,660 in its rate base, nor is there any evidence that any interest paid on any outstanding loans of the Utility to acquire these "unidentified assets" was included as an expense for ratemaking purposes. As part of the present proceeding, the Commission Staff audited the Utility's

books and found that the Utility has appropriately followed the Commission's 1992 ruling.

KPOG seems to believe that the ratepayers are in some way paying for the assets that were excluded. This is simply not the case. The assets were excluded from the rate base; therefore, they were not included in determining the rates that the customers would pay. Although the Utility, which is a privately owned company, paid for assets which were identified, both by engineers and accountants, the Commission disallowed this cost when determining an appropriate operating margin for the Utility. This cost has no financial effect on the rates and services provided to the Utility's customers. (Order 92-1030, p. 24-25) For the aforesaid reasons, this Commission's handling of this issue of "unidentified assets" from the 1992 rate case was appropriate and supported by substantial evidence in the record. Further, we believe that to the extent that KPOG reargues issues that were addressed in the 1992 case, it is collaterally estopped from relitigating them. See Bennett v. S.C. Dept. of Corrections, 305 S.C. 310, 408 S.E.2d 230 (1991) (the doctrine of collateral estoppel precludes a party from relitigation of the issues addressed by an agency in a prior proceeding involving the party). We therefore reject KPOG's assertions as to the so-called "unidentified assets."

(Q) Other Adjustments

Two other miscellaneous adjustments need to be discussed. Both Company and Staff propose an adjustment of ($340) to eliminate certain miscellaneous revenue. We agree and adopt the adjustment.

The Company and the Consumer Advocate proposed an adjustment of ($1,875) to transfer contributions to below-the-line, where such contributions normally appear for ratemaking purposes. Staff proposes ($2,549). We adopt the Company and Consumer Advocate adjustment as appropriate, since their number appears to more accurately reflect said contributions in this case.

We also hold that appropriate tax effects of all adjustments, including interest synchronization, have been calculated by the Staff in this case.

RATE BASE ITEMS

(A) Consulting Fees

In order to adjust the capitalization of consulting fees, the Staff proposes an adjustment of ($1,935) to accumulated depreciation and $82,335 to plant. We believe that this is appropriate ratemaking treatment for this capitalization, and therefore, adopts Staff's adjustment.

(B) Completed 1996 Additions

The Staff has proposed an adjustment to rate base for completed 1996 addition, and proposes an adjustment of ($520,628) to Construction Work in Progress (CWIP) and a $2,625,517 adjustment to plant. The Consumer Advocate proposes no rate base adjustment for this item. The company proposes and adjustment slightly different from the Staff's. However, we believe that the Staff's rate base adjustment is most appropriate for the completed 1996 additions, and therefore, adopts Staff's adjustments.

(C) Ocean Course

We believe that the Staff adjustment to rate base of $37,693 to accumulated depreciation and ($323, 642) to plant is appropriate to adjust rate base to exclude a portion of Ocean Course, as per Commission Order No. 92-1030.

(D) Cash Working Capital

With regard to cash working capital, the Company and the Staff propose the $1/8^{th}$ formula to calculate cash working capital. The Consumer Advocate proposes an alternate method which amounts to an offset with property taxes and income taxes. We have examined this matter, and believe that the Staff figure of $214,072 is an appropriate measure of cash working capital. We see no need to deviate from the formula method in this proceeding, and believe that it is appropriate for use in this case. We reject the Consumer Advocate's methodology, as we do not believe it may appropriately be applied in this case.

Consumer Advocate witness Miller stated that the lead-lag study is normally regarded as the most accurate method of determining cash working capital requirements. See Tr., Vol. 2, Miller at 171, lines 7-8. He further states that "however, for utilities with smaller cash working capital requirements, cash working capital is often determined on the basis of a formula method." See Tr., Vol. 2, Miller at 171, lines 17-18. The Commission agrees with the latter statement. In fact, we are of the opinion that no water or sewer utility operating under our jurisdiction warrants setting its cash working capital allowance based on the lead-lag study, which would be an additional expense to the utility for a time consuming study that, in our opinion, yields disputable results.

Further, Staff witness Maready testified that some of the property taxes are paid on a monthly basis, such as taxes on equipment, and are registered separately on the property records of the County. These expenses would affect the cash working capital allowance the same as any other expenses, such as wages. However, only the balance of the taxes, that is, those that are paid on an annual basis, would be subject to a lead-lag study. We are unable to ascertain the separate tax amounts that would be subject to the lead-lag study.

Further, we are not convinced that cash working capital allowance should be a combination of accounts i.e., some based on a formula method, and other accounts based on a different method, since some of the accounts mentioned by the Consumer Advocate are merely the result of a balance sheet approach. Each of the accounts are estimated each month and accrued, and in some instances, the estimated amounts are paid throughout the year. Since the accounts do appear on the balance sheet, then, the Consumer Advocate proposes that the Commission apply the lead-lag study to these accounts. The income statement, after approved adjustments for the test year ending December 31, 1995, shows a loss, and therefore, no income taxes. In fact, there were no income taxes, until after the new rates went into effect, which was in 1997, and even then, there was no guarantee that the Company would have taxable income at that time. Thus, the Consumer Advocate's approach in this case is not appropriate.

In this case, the decision on revenue requirements was based on operating margin, as opposed to a return on rate base, the latter requiring the computation of a rate base. Cash working capital allowance is an element of the rate base. Rate base was not needed

in this case, except to determine annualized interest and the income tax effect thereof. Any changes to cash working capital would not materially affect the operating margin in any case. In view of these issues concerning cash working capital, we believe that the Staff's proposal was the correct one, and that the Consumer Advocate's adjustment should be rejected.

(E) Tap Fees

The Consumer Advocate proposes to include tap fee costs for 1992 through 1995 in plant. The Consumer Advocate and KPOG also propose to include tap fee revenue from 1992 through 1995 as contributions in aid-of-construction. We have examined this matter, and do not agree that tap fee costs or tap fee revenues should be included in either plant or contributions in aid-of-construction at this time, since the costs of taps are not included in the Company's assets.

First, clearly, since no assets are included on the books with regard to tap fees, no subtraction from rate base as a contribution in aid of construction is appropriate. This is simply recognition of the matching principle. Further, more funds in this situation were contributed by the developer than by the ratepayer in the form of fees. We would note that there is nothing in the rules or chart of accounts about a company contributing such fees. Therefore, a tap fee may not necessarily be an asset on the books of the Company. If a tap fee is not an asset of the Company, then it does not need to be an off-setting entry in contributions in aid of construction. We note, however, that $122,500 was in revenues, and this was subtracted from revenues and added to the rate base as a contribution in aid of construction, which is the way we have handled this matter in prior

Orders in this case. We believe that this approach is appropriate in the present case as well, due to the contributed tap fees to this utility.

Mr. Clarkson, the chief operating officer for the Utility, testified that the tap-in fees for test year 1995 were included in the rate case and were treated as contribution in aid of construction, because the cost to the Utility usually associated with a tap closely equates with the tap fees collected. Tr., Vol. 1, Clarkson at 80. In fact, according to Mr. Clarkson, these costs for the installation of meters and other tap-in work "have been more than the fees if you look at them on average..." Id.

Thus, there is substantial evidence to support this Commission's decision to treat tap-in fees collected during the test year as contribution in aid of construction, to be consistent with the Commission's policy of handling tap fees. Further, since the fees and costs associated with performing the tap-in work "basically wash each other out" (Id), this Commission had evidence before it that justified not requiring the Utility to treat these fees during the interim years outside the test year as a contribution in aid of construction. Because there was evidence that the costs attributable to tap-ins equaled or exceeded the fees derived from them, not taking them into account in the interim years either as contributions in aid of construction or revenues/expenses does not materially alter the rate base to cause a material difference. Porter v. South Carolina Public Service Commission, ____ , S.C. ____ 489 S.E.2d 467 (1997).

(F) Eugenia Avenue Sewer Project

The Company has proposed the addition of $500,000 to plant for the construction of the Eugenia Avenue Sewer Project. It also proposes a ($30,871) adjustment to CWIP.

KPOG, the Consumer Advocate, Staff, and the Town of Kiawah propose that the Eugenia Avenue Sewer Project be disallowed. KPOG also proposes a ($30,871) adjustment to CWIP, accordingly. We have examined this matter, and agree with KPOG, the Consumer Advocate, Staff, and the Town of Kiawah that any monies be disallowed at this time. No construction has begun; therefore, this is not a known and measurable amount. Therefore, $500,000 proposed by the Company is disallowed.

We make no decision at this time regarding whether the project should be chargeable to all customers of Kiawah or only to the residents of Eugenia Avenue. We reserve this decision for another Order.

(G) Availability Fees/Building Incentive Fees

KPOG proposes to include availability fees/building incentive fees as contribution in aid-of-construction based on 1991 fees times 4% a year for the years 1992 through 1995, and therefore, proposes an adjustment of ($530,098). We disagree with KPOG. We hold that this is an improper method to include such fees as contribution in aid-of-construction. We therefore reject KPOG's adjustment.

First, we would note that, with regard to building incentive fees, we do not note any evidence in the record to show that such fees were being collected during the test year. Second, we would also note that, with regard to availability fees, $1.6 million was deducted from the rate base. See Hearing Exhibit 7, Adjustment No. 16, Exhibit A, p. 4. This is the gross amount. This appropriately recognizes availability fees, and in our opinion, is all that is necessary to do so.

To encourage construction of houses on the unimproved lots that it sells, the developer, KRA, assesses a building incentive fee against the owners of undeveloped lots. This fee is paid directly to KRA. The building incentive fee is entirely different from the availability fees that were once (but no longer) charged by KRA for infrastructure that included water and sewer lines.

KPOG would argue that the building incentive fee is the same as the water and sewer availability fees that were previously charged by KRA and that the Commission should have treated them as revenues of the Utility and that the Utility has acted contrary to the Commission's previous order in not including the current building incentive fee charged by KRA. Contrary to this argument, the record fully supports our findings and conclusions that current building incentive fees are not identical to the availability fees that were once charged and that the Utility abided by the Commission's prior order by taking into account the availability fees that were assessed years ago.

KPOG's witness, Mr. DuBois, stated that the Utility was in defiance of the Commission's order concerning availability fees. Tr., Vol. 2, DuBois at 133. In actuality, the Utility and the Commission's Staff concurred with the adjustment that was made based on the carry forward of the adjustment ordered by the Commission in its 1992 Order requiring that the prior availability fees paid to the Utility be treated as contribution in aid of construction. (Order No. 92-1030, p. 28-29) Mr. Clarkson's testimony that this adjustment had been made is uncontradicted. It is noted that the Commission Staff auditor, Joseph Maready, made the same adjustment for availability fees ($1,512,920) based upon the carry forward that was in place when the fees were collected prior to the

rate case in 1992. The Commission made an adjustment deducting $1,512,920 from the rate base. (Hearing Exhibit #7, Staff Accounting report, Adjustment No. 25, p. 7, and Order No. 97-151, p. 7.)

Furthermore, the Utility responded to the PSC Data Request No. 1-11 and 1-13 that no availability fees have been collected since 1991. Consistent with this proof, we noted that the contentions of the Petitioner were incorrect because there was no evidence in the record that any availability fees were collected by the Utility during the test year. Mr. Clarkson, the Utility witness, testified that the Utility does not receive any monies from building incentive fees that are collected by KRA. Tr., Vol. 1, Clarkson at 65-66; Tr., Vol. 2, Clarkson at 262-263. He further testified that none of the building incentive fees that are collected by KRA are related to the provision of water and sewer services on Kiawah Island. Tr., Vol. 1, Clarkson at 65-66. Therefore, the customers do not pay building incentive fees to the developer for the water and sewer lines, and then later have to pay the Utility for the same utility lines through their rates, which is the assertion of KPOG. Tr., Vol. 1, Clarkson at 66. We reject KPOG's proposal.

(H) Cost of Fire Hydrants

KPOG also proposes to exclude the cost of fire hydrants on distribution lines with associated adjustments to depreciation and interest expense, and that the developer be required to repay the utility. This would amount to a $13,968 adjustment to accumulated depreciation, and ($139,807) adjustment to plant. We disagree with this adjustment. We do not believe it is appropriate under the facts in the present case, and therefore reject the adjustment.

In the 1992 case, Mr. Bohannon, a civil engineer with extensive knowledge of the infrastructure of the Utility, prepared a report that was submitted into evidence in the 1992 rate case. It contains a table, entitled "Identifiable Transmission Lines and Appurtenances, Purchased by Kiawah Island Utility Company, Inc. from KRA on July 9, 1981. Reference: Thomas & Hutton Facilities Valuation Report, Dated June 17, 1991", listing the Utility's identifiable assets being purchased by the Utility, totaling $858,340.09 which includes the fire hydrants with a value of $158,900. (See Answers to PSC Data Request No. 2) In its 1992 Order, this Commission allowed the $858,340, including the fire hydrants as a legitimate cost to be included in the rate base as plant in service. (Order No. 92-1030, p. 24-25)

Just as in the 1992 case, Mr. Bohannon testified in this case that he prepared a study of transmission lines, fire hydrants, and appurtenances that were purchased by the Utility from the parent in 1996. The Utility paid the parent, on September 1, 1996, $805,795 for the transmission lines, fire hydrants, and appurtenances identified in the Thomas & Hutton report. Sixty-seven Thousand ($67,000) Dollars of this amount was attributable to the fire hydrants (Tr., Vol. 2, Bohannon at 13, 2-28 and Hearing Exhibit #3, Response to Kiawah Island Property Owners Group Third Set of Interrogatories No. 3-5a.) All of the fire hydrants were identified as to number and cost in the Thomas & Hutton report.

It is important to note that KPOG does not contend that the purchase price charged by KRA for the fire hydrants was too high or more than they were worth. KPOG also does not contest that the hydrants are essential to the services provided by the Utility

and provide income to the Utility. Rather, KPOG contends merely that the Utility should not have to pay for them.

This Commission rejects the Petitioner's proposed adjustment relating to fire hydrants, just as it did in the 1992 case. Despite KPOG's argument that developers often contribute fire hydrants at no charge to utility companies, we note that there is nothing in the Chart of Accounts nor any rule requiring a company to contribute fire hydrants. As was testified to in the unappealed 1992 rate case, the fire hydrants make money for the Utility; St. Johns Fire Department pays the Utility a service fee for each hydrant. Therefore, the hydrants are sources of revenue which benefit all Utility customers. In this case, the evidence showed that the annual rental income received from St. John's Fire Department totaled in excess of $26,000. (Hearing Exhibit #2, Answers to Interrogatories of Consumer Advocate's First Set of Interrogatories, No. 1-9(a))

Based upon the testimony and the evidence, the Commission had substantial evidence to approve the inclusion of the costs of fire hydrants in the rate base as plant-in-service.

Once again, the issues raised by KPOG that were addressed in the 1992 Order were not appealed, and therefor are also barred by law. Bennett v. S.C. Dept. of Corrections, supra. The Commission is not required to make factual findings of fees approved in a previous proceeding. Hamm v. South Carolina Pub. Serv. Comm'n and Carolina Water Service, Inc., 432 S.E.2d 454 (S.C. 1993).

(I) Transmission Lines

KPOG proposes that transmission lines included in completed CWIP be disallowed due to misclassification. The Consumer Advocate proposes not updating any CWIP beyond the test year. Staff and Company have proposed an adjustment of $805,795, which would transfer transmission lines in CWIP to plant in service. We have examined this matter, and believe that the Staff and Company position and adjustment are appropriate, and therefore, adopt same. We were not persuaded by the testimony of KPOG on this issue. KPOG's witness, Mr. Richard Sayers (who is not an engineer and has no utility operation background or experience) gave his personal opinion that Thomas & Hutton, the Utility's engineering firm, had incorrectly defined "transmission" and "distribution" lines. Tr., Vol. 2, Sayers at 45-46. We reject this analysis. We agree with the Staff and the Utility that these lines should simply be considered assets in the plant in service.

The controlling question is whether these transmission lines and hydrants were plant in service or not. It is undisputed that they were. Additionally, it is undisputed that the transmission lines were identified and paid for by the Utility. The Utility's engineer, Mr. Mitchell Bohannon, introduced into evidence and testified concerning the report that his engineering firm prepared on behalf of the Utility, explaining that each and every location of the transmission lines, fire hydrants, and related appurtenances were identified in its report. (Thomas & Hutton Report – Hearing Exhibit #3, Answers to Third Set of Interrogatories of KPOG, No. 3-5a.) The value of the lines, fire hydrants, and appurtenances were established in the Engineer's Report to be $805,795, and it is

undisputed that they are used and useful in the operation of the Utility. (Tr., Vol. 2, Bohannon at 13, 20-28.) KPOG does not contend that the sales price was too high; rather, it returns to its argument that the Utility should not have to pay for these assets.

KPOG states that some of the new areas being served are relatively remote and will not generate sufficient income on a stand-alone basis to cover the installation cost of providing service to them. One of the important points that KPOG overlooks in advancing this argument is that these new areas re all within the service district of the Utility. Hence, the Utility is obligated to furnish service. These new customers are entitled to the same treatment as existing customers who may occupy properties that are more conveniently located.

KPOG's principle argument about these expenses, though, rests on its contention that all lines on Kiawah Island should, in its estimation, be classified as distribution lines and, as such, be furnished and donated by the developer, KRA. Mr. Sayers, a property owner, who was not testifying as an expert witness, gave his view that the engineering firm, Thomas & Hutton, had incorrectly defined "transmission" and "distribution" lines. Mr. Sayers gave his personal opinion that basically all of the lines on Kiawah Island are distribution lines, and should be constructed, paid for, and donated by the developer, KRA, to the Utility. Tr., Vol. 2, Sayers at 64-68.

Mr. Bohannon, a licensed civil engineer who did testify as a qualified expert, testified that based upon the American Waterworks Association guidelines that his firm uses to classify transmission and distribution lines, the lines are correctly classified on Kiawah as either transmission or distribution lines. Tr., Vol. 2, Bohannon at 26. Under

this analysis, transmission lines are the financial responsibility of the Utility. When the developer pays for and constructs distribution lines, they are donated to the Utility as contribution in aid of construction. Thomas & Hutton's report shows that the developer, KRA, paid $1,200,000.00 for the construction of distribution lines, which were donated to the Utility, and treated as contribution in aid of construction.

In conclusion, the Commission's decision to include the expense associated with the recently acquired transmission lines and hydrants is supported by the evidence of record. The lines are plant in service being used by the Utility. Additionally, even if the Commission had decided to embark on analysis that turned on whether the lines in question were distribution or transmission lines, as argued by the Petitioner, the record would fully support the finding and conclusion that they were transmission lines that would have to be paid for by the Utility. The Commission's and Utility's treatment of the transmission lines as plant in service, is in accordance with generally accepted engineering practices and standards and is consistent with the rules of the Commission in its 1992 Order.

Finally on this item, this court would note that the South Carolina Supreme Court, in the case of Peoples Natural Gas Company of South Carolina v. South Carolina Pub. Serv. Comm'n, 298 S.C. 347, 380 S.E.2d 825 (S.C. 1989), held:

> The Public Service Commission is recognized as the 'expert' designated by the legislature to make policy [298 S.C. 348] determination regarding utility rates; thus, the role of a court reviewing such decisions is very limited. We decline to make any legal distinction between transmission service and distribution service. Any such distinction will have to be made, if at all, by the Public Service Commission or the Legislature.

In this case, we decline to draw a distinction between the transmission and distribution lines, as set forth in our Order. Comparing the conflicting testimony presented by Mr. Sayers, a property owner, who was not testifying as an expert witness, and the expert testimony of Mr. Bohannon of Thomas & Hutton, this Commission has substantial evidence to support its findings that these items constituted plant in service and that their cost should be included in the rate base.

(J) Cross Collateralization/Cross Default

In an unusual request, KPOG requests that the Commission re-write the Utility's agreements for financing its operations with NationsBank to eliminate the cross collateralization and cross default provisions. NationsBank has made loans to both the Utility and KRA. The loan agreements have as collateral the assets of both KRA and the Utility. They also specify that a default by one of the entities constitutes a default by the other. Mr. Clarkson testified that NationsBank required this cross collateralization of the assets of both the parent company and the Utility. Tr., Vol. 1, Clarkson at 63-64; Tr., Vol. 2, Clarkson at 257.

Mr. Clarkson testified also that the Utility is an asset that was collateral for the original acquisition and development loan when Kiawah Island and the Utility were purchased from the Kuwaitis in 1988. Tr., Vol. 1, Clarkson at 64. In the most recent loan documents, KRA had to use its real estate collateral to support a loan to the Utility. If the Utility fails to make a payment, the bank can foreclose on the parent company's assets. Mr. Clarkson testified that the bank did not rely on the Utility and its income

stream for collateral for the loan to the Utility, but rather relied on the real estate assets of the parent company for collateral.

Without the strong financial backing of the parent company and its willingness to pledge its real estate as collateral for the Utility's loans, the Utility would not be able to obtain the loans necessary to construct the capital projects that the Utility must construct in order to service customers. As Mr. Clarkson testified, the real estate assets of KRA that are pledged are much more valuable than those of the Utility. (Tr. Vol. 1, Clarkson at 64; Tr., Vol. 2, Clarkson at 257.) The cross-collateralization required by NationsBank has benefited the Utility and has never had a negative effect. These loan provisions are commercially responsible and were necessary for the Utility to obtain financing for necessary expenses.

There is no proof in the record that the cross collateralization/cross default provisions of the NationsBank loan are detrimental to the Utility's being able to provide quality utility services to its customers at a reasonable rate.

(K) Treatment Cell No. 2

KPOG asserts that Treatment Cell No. 2 is a holding pond for effluent only, and that certain costs should be disallowed until utilization as a treatment cell occurs. KPOG requests an adjustment of ($373,053). We disagree with the proposed adjustment. We believe that Treatment Cell No. 2 is used and useful in Kiawah's sewer operations. We therefore reject the adjustment.

All other adjustments inconsistent with the above are hereby deemed denied, as are other items proposed by KPOG having to do with interest rate, developer's debt and

the bank agreement, alleged overstatement of the 1992 rate case, the change in the classification of transmission and distribution lines, and the proposal for an impact fee. We are simply not persuaded by the testimony on these matters.

Based on the accounting and proforma adjustment herein approved, the Company's appropriate total income for return for the computation of an appropriate operating margin is $102,360. The calculation of total income for return is shown in Table A.

TABLE A
TOTAL INCOME FOR RETURN – AS ADJUSTED

Operating Revenues	$ 2,886,199
Operating Expenses	2,306,237
Net Operating Income	579,962
Customer Growth	10,207
Less Interest	(487,809)
Total Income for Return	102,360

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 13 AND 14.

Under the guidelines established in the decisions of Bluefield Waterworks and Improvement Company v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas, 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will produce net revenues. As the United States Supreme Court noted in the Hope Natural Gas decision, supra, the utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgement and giving consideration to all relevant facts, the Commission should establish

rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and ... that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

Neither S.C. Code Ann. Section 58-5-240 (Supp. 1995) nor any other statute describes a particular method to be utilized by the Commission to determine the lawfulness of the rates of a public utility. For ratemaking purposes, this Commission examines the relationships between expenses, revenues, and investment in a historic test period because such examination provides a constant and reliable factor upon which calculation can be made to formulate the bases for determining just and reasonable rates. This method was recognized and approved by the South Carolina Supreme Court for ratemaking purposes involving utilities in Southern Bell Telephone and Telegraph Company v. The Public Service Commission of South Carolina, 270 S.C. 590, 240 S.E.2d 278 (1978).

For water and sewer utilities, the Commission may decided to use the "operating margin" as a guide in determining just and reasonable rates, instead of examining the utility's return on its rate base. The operating margin is determined by dividing total income for return (or net operating income) by the operating revenues of the utility.

The Commission finds that its use of the operating margins has resulted in fair rates to both the utility and the ratepayer. In this proceeding, the Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates, and the fixing of just and reasonable rates. This method was recognized

as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 S.E.2d 257 (1984). The following Table indicates the Company's gross revenues for the test year under the presently approved rate schedules; the Company's operating expenses for the test year; and the operating margin under the presently approved schedules for the test year:

TABLE B
OPERATING MARGIN – AS ADJUSTED

Operating revenues	$2,650,861
Operating Expenses	2,248,827
Net Operating Income	402,034
Customer Growth	7,076
Less Interest	(487,809)
Total Income for Return	(78,699)
Operating Margin After Interest	(2.97%)

The Commission is mindful of those standards delineated in the Bluefield decision, supra, and of the balance between the respective interests of the Company and of the consumer. The Commission has considered the spectrum of relevant factors in this proceeding, including, among others: the revenue requirements for the Company, the price for which the Company service is rendered, as well as the proposed price, the quality of the service, and the effect of the proposed price upon the consumer.

The three fundamental criteria of a sound rate structure have been characterized as follows:

> ...(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the

> optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships between costs incurred and benefits received.
>
> Bonbright, Principles of Public Utility Rates, (1961), p. 292.

The Commission has considered the proposed increase presented by the Company in light of the various standards to be observed and the interests represented before the Commission. The Commission has also considered the impact of the proposed increase on the ratepayers of the Company. The Commission must balance the interest of the Company – the opportunity to make a profit or earn a return on its investment, while providing adequate water service – with the competing interest of the ratepayers – to receive adequate service at a fair and reasonable rate. In balancing these competing interests, the Commission has determined that the proposed schedule of rates is unjust and unreasonable and inappropriate for both the Company and its ratepayers.

In light of those factors as previously discussed, and based upon the record in the instant proceeding, the Commission concludes that a fair operating margin that the Company should have an opportunity to earn is 3.55% which requires annual operating revenue of $2,886,119. The following Table reflects an operating margin of 3.55%:

TABLE C
OPERATING MARGIN – AS APPROVED

Operating Revenues	$2,886,199
Total Expenses	2,306,237
Net Operating Income	579,962
Customer Growth	10,207
Less Interest	(487,809)
Total Income for Return	102,360
Operating Margin (After Interest)	3.55%

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 15 AND 16.

The Commission concludes that while an increase in rates is necessary, the proposed increase is unreasonable and inappropriate. Accordingly, the Commission will design rates which will increase the proposed commodity charge for the customers. No increase in the Company's basic facilities charge is granted. We believe that any increase in rates ought to be based on actual usage of water. We note that very little of the granted increase will therefore be applicable to Kiawah Island's part time residents, but will be applicable to those who utilize the water system over a greater period during the year.

We do not believe that the Company has justified an increase in its tap fees.

The Company proposed to automatically pass through price changes from St. John's Water Company to Kiawah Island Utility, Inc., pursuant to the Company's contract with St. John's Water Company. Accordingly, whenever a price adjustment to the Company is forwarded by St. John's, the Company would propose to increase the unit price of potable water sales to all customer classes by the amount of that increased cost. At the same time, if the delivered unit price is decreased by St. John's, the Company would pass that decrease on to its customer classes. In Order No. 92-1030 at 36, we determined that this automatic pass through of any price changes from St. John's Water Company was inconsistent with the requirement that the Commission not allow rates or tariffs to be put into effect without a hearing, if the changes resulted in a rate increase to the utility. This was consistent with the requirements of S.C. Code Ann. Section 58-5-240. We believe that this is still a valid holding, and we deny the Company's proposal accordingly.

The rate designs and rate structures approved by this Commission as depicted in Appendix A attached hereto and incorporated by reference are approved and effective for purposes of this Order. We believe that the rates and charges approved herein achieve a balance between the interests of the Company and those of its customers. These rates and charges result in a reasonable attainment of the Commission ratemaking objectives in light of applicable statutory safeguards.

As a caveat, it should be noted that this Order is not intended to supercede Commission Order Nos. 99-216 and 99-349 in Docket No. 98-328-W/S, which address the present rates of Kiawah Island Utility, Inc., but is merely intended to address the September 7, 1999 Order of the South Carolina Supreme Court, which basically called for a new written Order in Docket No. 96-168-W/S. The purpose of this Order is to comply with the Supreme Court's directive, while not superceding our rate Orders issued in Docket No. 98-328-W/S. The Company's present approved rates are still found in Order No. 99-216 and 99-349.

IT IS THEREFORE ORDERED THAT:

1. The proposed schedule of rates and charges as filed in the Company's 1996 Application is found to be unreasonable, and is hereby denied.

2. The schedule of rates and charges attached hereto as Appendix A is hereby approved for purposes of this Order only. The schedule is deemed filed with the Commission pursuant to S.C. Code Ann. Section 58-5-240 (Supp. 1995).

3. The Company shall maintain its books and records in accordance with the NARUC Uniform System of Accounts as adopted by this Commission.

4. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Chairman

ATTEST:

Executive Director

(SEAL)

Appendix A

KIAWAH ISLAND UTILITY, INC.
31 Sora Trail Rd.
Johns Island, SC 29455
(843) 768-0641

FILED PURSUANT TO DOCKET NO. 96-168-W/S – ORDER NO. 2000-713
EFFECTIVE DATE: SEPTEMBER 1, 2000

SCHEDULE OF RATES AND CHARGES

RATE SCHEDULE NO. 1

RESIDENTIAL SERVICE

AVAILABILITY -- Available within the Company's certificated service area.

APPLICABILITY -- Applicable to any residential customer for any purpose.

CHARACTER OF SERVICE – Water and sewer service

CHARGES –

Water Service Charges

	Monthly Consumption	Water Rate
A.	Minimum Bill 0 - 2,000 gal/mo.	
	5/8" meter	$ 18.00/mo.
	3/4" meter	$ 30.00/mo.
	1" meter	$ 50.00/mo.
	1 ½ " meter	$100.00/mo.
	2" meter	$160.00/mo.
	3" meter	$350.00/mo.

Minimum Water Service Charge for meters larger than 3" shall be:

Maximum recommended meter capacity *(gpm)* x $18.00 per mo.
20 gpm

B.	Consumption Charge All over 2,000 gal./mo.	$ 2.10/1000 gal.

Sewer Service Charges

A flat rate of $22.00/mo.

TAP FEES --	Water tap-in fee	$500.00
	Sewer tap-in fee	$500.00

The tap-in fee provides for installation of the normal size residential meter of 5/8" by 3/4". Where the customer requests a larger meter, Company will apply the tap-in fee schedule for larger meters as listed in the *Commercial Service Schedule No. 2.*

RATE SCHEDULE NO. 2

COMMERCIAL SERVICE

AVAILABILITY -- Available within the Company's certificated service area.

APPLICABILITY -- Available to any Commercial or Master Metered Residential Customer for any purpose except Hotel or Motel use (see Rate Schedule No. 3).

Water Service Charges

A. Basic Facilities Charge

5/8" meter	$ 18.00/mo.
3/4" meter	$ 30.00/mo.
1" meter	$ 50.00/mo.
1 ½" meter	$100.00/mo.
2" meter	$160.00/mo.
3" meter	$350.00/mo.

Basic Facilities Charge for water service with meters larger than 3" shall be:

$$\frac{\text{Maximum recommended meter capacity (gpm) x \$18.00 per mo.}}{\text{20 gpm}}$$

B. Consumption Charge — $2.10/1000 gal. for all consumption

Sewer Service Charges

A.	Basic Facilities Charge	
	5/8" meter	$ 18.00/mo.
	3/4" meter	$ 27.75/mo.
	1" meter	$ 46.25/mo.
	1 ½" meter	$ 92.50/mo.
	2" meter	$148.00/mo.
	3" meter	$323.75/mo.

Basic Facilities Charge for sewer service where water service is through meters larger than 3" in size shall be:

$$\frac{\text{Maximum recommended meter capacity } (gpm) \times \$18.00 \text{ per mo.}}{20 \text{ gpm}}$$

B. Consumption Charge — $ 1.80/1000 gal. for all consumption

Tap Fees

Tap-in Fees		Water Tap-in Fee	Sewer Tap-in Fee
5/8"	meter	$ 500.00	$ 500.00
3/4"	meter	$ 750.00	$ 750.00
1"	meter	$1,250.00	$1,250.00
1 ½"	meter	$2,500.00	$2,500.00
2"	meter	$4,000.00	$4,000.00
3"	meter	$8,750.00	$8,750.00

Water Tap-in Fee and Sewer Tap-in Fee for water and sewer service where the water meter is larger than 3" in size shall be:

$$\frac{\text{Maximum recommended meter capacity (gpm)} \times \$500.00}{20 \text{ gpm}}$$

RATE SCHEDULE NO. 3

HOTEL AND MOTEL SERVICE

AVAILABILITY -- Available within the Company's certificated service area.

APPLICABILITY -- Applicable to all hotel and motel customers for any purpose.

Water Service Charges

Basic Facilities Charge	$8.00/mo/room
All Consumption	$2.10/1000 gal

Sewer Service Charges

Basic Facilities Charge	$7.50/mo/room
All Consumption	$1.80/1000 gal

Tap Fees

Water Tap-in Fee	$220/room
Sewer Tap-in Fee	$220/room

RATE SCHEDULE NO. 4

IRRIGATION SERVICE

AVAILABILITY -- Available within the Company's certificated service area. The Company reserves the right to limit or reduce the amount of irrigation service available when, in its sole judgment, its water system conditions require such restrictions.

APPLICABILITY -- Applicable only to customers who anticipate substantial potable water use which will not be returned to the Company's wastewater treatment system such as irrigation. Such water consumption shall be metered separately from any water use supplied under other rate schedules.

CHARGES --

Water Service Charges

A. Basic Facilities Charge

5/8" meter	$ 18.00/mo.
3/4" meter	$ 30.00/mo.
1" meter	$ 50.00/mo.
1 ½" meter	$100.00/mo.
2" meter	$160.00/mo.
3" meter	$350.00/mo.

Basic Facilities Charge for water service with meters larger than 3" shall be:

$$\frac{\text{Maximum recommended meter capacity (gpm)}}{20 \text{ gpm}} \times \$18.00 \text{ per mo.}$$

B.	Consumption Charge	$ 2.40/1000 gal. for all consumption

Tap Fees

5/8"	meter	$ 500.00
3/4"	meter	$ 750.00
1"	meter	$1,250.00
1 1/2"	meter	$2,500.00
2"	meter	$4,000.00
3"	meter	$8,750.00

Water Tap-in Fee where the water meter is larger than 3" shall be:

$$\frac{\text{Maximum recommended meter capacity (gpm) x \$500.00}}{\text{20 gpm}}$$

RATE SCHEDULE NO. 5

FIRE HYDRANT SERVICE

AVAILABILITY -- Available within the Company's certificated service area.

APPLICABILITY -- Applicable to fire hydrants connected to the water mains of the Company.

CHARGES -- $75.00 per hydrant per year payable semiannually in advance for fire fighting service. When temporary water service from a hydrant is requested by a contractor or others a meter will be installed and the charge will be:

$8.00 for each day of use PLUS $2.40/1000 gals. for ALL water used.

RATE SCHEDULE NO. 6

GOLF COURSE IRRIGATION

AVAILABILITY -- Available within the Company's certificated service area.

APPLICABILITY -- Applicable for golf course irrigation where the customer agrees to take as a minimum quantity the treated effluent from the wastewater treatment plant.

CHARGES –

A. Water, the source of which is the effluent from the sewerage collection system and which has been processed through the wastewater treatment plant, will be billed at the rate of:

Basic Facilities Charge	$164.00/mo.
Consumption	$ .40/1000 gal.

B. The deep well water will be billed at the rate of:

Basic Facilities Charge	$164.00/mo.
Consumption	$ 1.10/1000 gal.

C. Potable water will be billed at the rate of:

Basic Facilities Charge	$164.00/mo.
Consumption	$ 2.40/1000 gal.

CHARGES FOR SERVICE DISCONTINUANCE, RECONNECTION AND OTHER MISCELLANEOUS SERVICE CHARGES

CHARGES

1. When a customer requests temporary discontinuance of service for the apparent purpose of eliminating the minimum bill, during such cut-off period the Company may make a charge equivalent to a three months minimum bill for both water and sewer service and require payment of such charge before service is restored.

2. Temporary discontinuance of service for such purposes as maintenance or construction will be made and the Company may charge the customer the actual cost plus 25%.

3. Whenever service is disconnected for violation of rules and regulations, nonpayment of bills or fraudulent use of service, the Company may make a charge of $25.00 for water and $100.00 for sewer before service is restored.

4. Whenever service has been disconnected for reasons other than set forth in (3) above, and the Company is required to reconnect service to a unit that has had the service disconnected, the Company shall have the right to charge a $25.00 reconnection fee for restoration of service after 4:30 p.m. Monday through Friday or Saturday and Sunday.

5. Delinquent Notification Fee - $5.00. A fee of $5.00 shall be charged each customer to whom the Company mails a notice of discontinuance of service as required by the Commission rules prior to service being discontinued. This fee assesses a portion of the clerical and mailing costs of such notices to the customers creating that cost.

6. Customer Account Charge - $25.00. One-time fee charged to each new account to defray costs of initiating service.